

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
ROLAND AND SUSAN BECK	:	DETERMINATION
for Redetermination of a Deficiency or for Refund of	:	DTA NO. 829765
Personal Income Tax under Article 22 of the Tax Law	:	
for the Years 2015 and 2016.	:	

Petitioners, Roland and Susan Beck, filed a petition for redetermination of a deficiency or for refund of personal income tax under article 22 of the Tax Law for the years 2015 and 2016.

On December 2, 2021 and December 28, 2021, respectively, petitioners appearing by Barclay Damon LLP (David G. Burch, Jr., Esq., of counsel), and the Division of Taxation, appearing by Amanda Hiller, Esq. (Christopher O'Brien Esq., of counsel), waived a hearing and submitted this matter for determination based upon documents and briefs to be submitted by September 2, 2022, which date commenced the six-month period for issuance of this determination. After due consideration of the documents and arguments submitted, Winifred M. Maloney, Administrative Law Judge, renders the following determination.

ISSUE

Whether, for purposes of computing the Qualified Empire Zone Enterprise tax reduction credit under Tax Law § 16 for resident shareholders of a New York S corporation, the Division of Taxation properly multiplied the S corporation's business allocation percentage by petitioners' income from the S corporation in calculating the tax factor component of such credit.

FINDINGS OF FACT

The parties entered into a stipulation of facts, dated December 2, 2021, in connection with this matter. Such stipulated facts have been substantially incorporated into the findings of fact set forth herein.

1. Tessy Plastics Corporation (Tessy Plastics) is an injection mold plastics manufacturer with its global headquarters based in Skaneateles, New York, and with manufacturing and warehouse facilities located in Elbridge, Van Buren and Auburn, New York.

2. Tessy Plastics is a company that specializes in the development and manufacture of products for the medical, consumer, electrical and business machine markets, with both a national and international customer base.

3. Tessy Plastics is a New York corporation that elected to be taxed under Subchapter S of the Internal Revenue Code (IRC).

4. Tessy Plastics is certified in the Onondaga County Empire Zones Program with an effective eligibility date of December 17, 2003.¹ Tessy Plastic is a qualified empire zone enterprise (QEZE).

5. The corporate tax returns for Tessy Plastics for the 2015 and 2016 tax years were prepared by Fust Charles Chambers LLP and included the form 1120S US income tax return for an S corporation (Form 1120S), and the CT-3-S New York S corporation franchise tax return (CT-3-S return). As part of its CT-3-S returns filed for tax years 2015 and 2016, Tessy Plastic claimed certain empire zone credits.

6. Roland Beck is the President and majority shareholder, either directly or through his grantor trust, in Tessy Plastics.

¹ Tessy Plastics has two empire zone locations under its Onondaga County empire zone certification, facilities located in the towns of Elbridge and Van Buren.

7. Petitioners, Roland and Susan Beck, filed joint form IT-201, New York State resident income tax returns (personal income tax returns) for tax years 2015 and 2016. Petitioners claimed empire zone credits, including the QEZE tax reduction credit on their 2015 and 2016 personal income tax returns.

8. As reported on schedule K-1 of form 1120S and schedule B of the CT-34-SH, New York S corporation shareholders' information schedule, attached to and made a part of the CT-3-S return, Roland Beck, directly and through the Roland G. Beck 2015 Retained Annuity Trust, owned 67.1025% of the stock of Tessy Plastics in tax years 2015 and 2016.

9. As shown on the form CT-604, claim for QEZE tax reduction credit, filed with Tessy Plastics' 2015 CT-3-S return, all employees of Tessy Plastics working at its New York locations were situated at empire zone locations in 2015.

10. On schedule D – zone allocation factor of the form CT-604 filed with its 2015 CT-3-S, Tessy Plastics reported approximately \$110 million of its \$119 million in New York assets were situated at empire zone locations in 2015, a 92.32% EZ property factor and a zone allocation factor of .9616, and reduced its calculated QEZE tax reduction credit accordingly.

11. As shown on the form CT-604 filed with its 2016 CT-3-S return, approximately 78.5% of Tessy Plastics' employees working at its New York locations were situated at empire zone locations in 2016. On schedule D – zone allocation factor of the form CT-604, Tessy Plastics reported a 78.52% EZ payroll factor and a zone allocation factor of .8508, and reduced its calculated QEZE tax reduction credit for tax year 2016 accordingly.

12. The 2015 form CT-604 claim for QEZE tax reduction credit (form CT-604-2015) reported the following factors for the calculation of the QEZE tax reduction credit:

(a) schedule C of the form CT-604-2015 calculated the employment increase factor of 1.0 based upon 385.5 empire zone employees for the test year employment number and 813.25 empire zone employees in the 2015 tax year;

(b) schedule D of the form CT-604-2015 calculated the zone allocation factor of 0.9616 based upon 92.32% of the NY assets owned by Tessy Plastics situated at the empire zone locations as opposed to elsewhere in New York State, and all of Tessy Plastics' payroll occurring at the empire zone locations as opposed to elsewhere in New York State; and

(c) schedule E of the form CT-604-2015 calculated the benefit period factor of 0.4 based upon the tax year being the 13th year of the business tax benefit period.

13. The 2016 CT-3-S return filed for Tessy Plastics included the form CT-604 claim for QEZE tax reduction credit (form CT-604-2016) that reported the following factors for the calculation of the QEZE tax reduction credit:

(a) schedule C of the form CT-604-2016 calculated the employment increase factor of 1.0 based upon 385.5 empire zone employees for the test year employment number and 895.5 empire zone employees in the 2016 tax year;

(b) schedule D of the form CT-604-2015 calculated the zone allocation factor of 0.8508 based upon 91.63% of the NY assets owned by Tessy Plastics situated at the empire zone locations as opposed to elsewhere in New York State, and 78.52% of Tessy Plastics' payroll occurring at the empire zone locations as opposed to elsewhere in New York State; and

(c) schedule E of the form CT-604-2016 calculated the benefit period factor of 0.2 based upon the tax year being the 14th year of the business tax benefit period.

14. Tessy Plastics provided Mr. Beck with multiple Federal schedule K-1s for the 2015 and 2016 tax years, reporting the amount of ordinary income, interest income, and other income

allocated to Mr. Beck based upon his percentage of stock ownership both directly and through The Roland G. Beck 2015 Retained Annuity Trust.

15. Tessy Plastics provided Mr. Beck with multiple New York schedule K-1 equivalents for the 2015 and 2016 tax years, individually and for The Roland G. Beck 2015 Retained Annuity Trust, reporting the benefit period factor, employment increase factor and zone allocation factor to be used in the calculation of petitioners' QEZE tax reduction credit to be claimed on their New York State income tax returns; and also reporting any additions or subtractions to the federal income tax allocation based upon New York State tax laws.

16. The information provided on the Federal and New York State schedule K-1s was used by the petitioners to calculate the QEZE tax reduction credit claimed on petitioners' personal income tax returns for the years 2015 and 2016.

17. The business allocation percentage (BAP) reported by Tessy Plastics on its CT-3-S returns was 19.7574% for tax year 2015 and 21.3694% for tax year 2016.

18. The business allocation percentages are not provided by Tessy Plastics to its shareholders on either the Federal schedule K-1 or the New York schedule K-1 equivalent.

19. Petitioners filed their form IT-604 claim for QEZE tax reduction credit through Tessy Plastics for the 2015 tax year (form IT-604-2015), and under schedule E of the form IT-604, calculated the tax factor component of the QEZE tax reduction credit. The resulting tax factor was \$2,003,615.00.

20. Petitioners filed their form IT-604 claim for QEZE tax reduction credit through Tessy Plastics for the 2016 tax year (form IT-604-2016), and under schedule E of the form IT-604, calculated the tax factor component of the QEZE tax reduction credit. The resulting tax factor was \$1,992,303.00.

21. Line 21 of the form IT-604 states “Enter the amount of your income from the QEZE allocated within NYS (*see instructions*).” The instructions for line 21 specific to shareholders of New York S corporations that are QEZEs as set forth on the IT-604-I state:

“This is the income from the New York S corporation that is a QEZE, allocable to New York State and included in New York adjusted gross income. Do not include any wages paid to you by the New York S corporation. The income allocable to New York State is the QEZE S corporation’s income from New York State sources. This amount should be provided to you by the New York S corporation.”

22. All income reported on line 21 of the form IT-604 that petitioners filed for tax years 2015 and 2016 was income from Tessy Plastics and included in their New York adjusted gross income (AGI) for tax years 2015 and 2016.

23. Petitioners calculated their QEZE tax reduction credit in schedule F on each individual form IT-604 as the product of their tax factor from line 24, and (i) the benefit period factor, (ii) the employment increase factor, and (iii) the zone allocation factor as provided by Tessy Plastics. The resulting QEZE tax reduction credit was \$770,670.00 for tax year 2015 and \$339,010.00 for tax year 2016.

24. Correspondence from the Division of Taxation (Division) dated August 21, 2017, addressed to petitioners and referencing Case ID# X-006063903 for the 2015 tax year, requested information for the calculation of multiple empire zone tax credits, including the QEZE tax reduction credit. With respect to the QEZE tax reduction credit, the Division’s letter stated the following:

“[Tax Appeals] Tribunal decision² 825436 stated that Tax Law section 16(f)(2), which contemplates an entity level allocation of the income of the enterprise, is reasonable. Therefore, since the allocation is required under the statute, the BAP is to be applied to the taxpayers [sic] QEZE income in the calculation of the tax factor.

² The Tax Appeals Tribunal decision referenced by the Division is *Matter of Purcell*, Tax Appeals Tribunal, November 14, 2016.

In 2015 Tessy Plastics Corporation had a 19.7574% BAP. Provide a calculation of your QEZE income allocated to NYS used in the calculation of the tax factor which applies the 2015 entity BAP.”

25. Correspondence from petitioners’ representatives, Barclay Damon LLP (Barclay Damon), to the Division dated November 17, 2017, provided the requested documentation for the calculation of the empire zone tax credits and stated that since petitioners as resident taxpayers were required to include all of their income passed through from Tessy Plastics in their New York adjusted gross income, all of their income was included in the calculation of the QEZE tax reduction credit.

26. Correspondence from the Division dated December 5, 2017, addressed to petitioners and referencing Case ID# X-774353554 for the 2015 tax year (the 2015 Audit Adjustment letter), set forth that the Division reduced petitioners’ QEZE tax reduction credit from \$770,670.00 to \$152,279.00 due to the application of the 19.7475% BAP to petitioners’ QEZE income. The letter indicated that adjustments were made to petitioners’ form IT-604, QEZE tax reduction credit, and form IT-603, EZ investment tax credit and employment incentive credit (form IT-603 credit). It further indicated that the form IT-603 credit applied to tax was increased by \$618,391.00 to fully offset the adjustment to the QEZE tax reduction credit, and petitioners’ carryforward of the form IT-603 credit to tax year 2016 was reduced to \$3,858,939.00.

27. The 2015 Audit Adjustment letter included schedules that reported the benefit period factor of 0.4, the employment increase factor of 1.0000 and the zone allocation factor of 0.9616 as set forth in finding of fact 12 above, and consistent with the form CT-604-2015 as filed.

28. On December 12, 2017, the Division issued to petitioners an account adjustment notice – personal income tax for tax year 2015 (December 12, 2017 account adjustment notice)

that separately recomputed petitioners' claimed overpayment to be \$188,571.00 based upon the adjustments attributable to the corrected BAP for tax year 2015.

29. Correspondence from the Division dated November 15, 2017, addressed to petitioners for the 2016 tax year, requested information for the calculation of multiple tax credits, and requested information as to the method of petitioners' "computation for the income from the QEZE allocated within NYS reported on line 21 of form IT-604 and [their] New York State AGI reported on line 22 of form IT-604."

30. Correspondence from Barclay Damon to the Division dated March 6, 2018, provided the requested documentation for the calculation of various tax credits, including the total income from Tessa Plastics included in petitioners' New York adjusted gross income.

31. Correspondence from the Division dated April 4, 2018, addressed to petitioners and referencing Case ID# X-006577693 for the 2016 tax year (the 2016 Audit Adjustment letter), set forth that the Division reduced petitioners' QEZE tax reduction credit from \$339,010.00 to \$72,436.00 due to the application of the 21.3694% BAP to petitioners' QEZE income. The 2016 Audit Adjustment letter indicated that in order to offset the reduction to petitioners' QEZE tax reduction credit an additional \$266,574.00 of the EZ investment tax credit was utilized. It also indicated that petitioners' carryforward of the EZ investment tax credit had been reduced as a result to \$2,421,190.00, and that petitioners should update their records accordingly. The Division considered the 2016 Audit Adjustment letter to be a notice of disallowance.

32. The 2016 Audit Adjustment letter included schedules that reported the benefit period factor of 0.2, the employment increase factor of 1.0000 and the zone allocation factor of 0.8508 as set forth in finding of fact 13 above, and consistent with the form CT-604-2016 as filed.

33. Section 16 of the New York State Tax Law provides that the QEZE tax reduction credit is equal to “the product of (i) the benefit period factor, (ii) the employment increase factor, (iii) the zone allocation factor and (iv) the tax factor” (*see* Tax Law § 16 [b]).

34. Pursuant to the instructions set forth on pages 2 and 3 of the CT-604-I (2015), a New York S corporation qualifying for a QEZE tax reduction credit is required to provide each shareholder with the three factors including (i) the benefit period factor, (ii) the employment increase factor, (iii) the zone allocation factor. The fourth factor, the tax factor, is computed by the shareholders on form IT-604 that is filed with their personal income tax returns.

35. Pursuant to page 5 of the IT-604-I (2015), shareholders of New York S corporations that are QEZEs determine the tax factor using the income from the New York S corporation that is a QEZE, allocable to New York State and included in New York adjusted gross income. It further states that the income allocable to New York State is the QEZE S corporation’s income from New York State sources. This amount is provided to the shareholders by the New York S corporation.

36. The form CT-604 does not request or report the amount of sales of New York tangible personal property nor does it request or report the amount of sales of tangible personal property outside of New York.

37. The form CT-604 does not request or report the business allocation percentage, nor does it require that this information be provided to the shareholders as part of the information for the calculation of the QEZE tax reduction credit.

38. The BAP for the 2015 and 2016 tax years as reported on the CT-3-S returns for Tessy Plastics is predicated solely upon the ratio of sales of New York State tangible personal property to all sales of tangible personal property. The location of property and employees does

not factor into the calculation of the BAP, and the BAP does not impact the taxable income for a resident taxpayer.

39. On audit, the Division applied the BAP of Tessy Plastics as a component of the tax factor calculation, and thereby reduced petitioners' QEZE tax reduction credit by \$618,391.00 in 2015 and by \$266,574.00 in 2016.

CONCLUSIONS OF LAW

A. In 1986, the legislature enacted New York State's Economic Development Zones (the EDZ Program). The purpose of the program was to stimulate private investment, private business development, and job creation in targeted geographic areas characterized by persistent poverty, high unemployment, shrinking tax bases and dependence upon public assistance (*see* General Municipal Law § 956). The EDZ Program offered a variety of state tax incentives designed to attract new businesses to the state and to enable existing businesses to expand and create more jobs (*see id.*). Over time, the EDZ Program gradually shifted its focus from poverty reduction to business development by relaxing eligibility requirements, and the program was changed to the Empire Zones Program Act in May of 2000 (L. 2000, ch. 63, part GG).

B. Businesses located in qualifying empire zone areas and that otherwise meet the statute's criteria could apply to the Department of Economic Development for a certificate of eligibility that they could then submit to the Department of Taxation and Finance in support of their claim for tax credits. These businesses are also referred to as QEZEs (*see* General Municipal Law § 959 [a]). As a certified QEZE, Tessy Plastics was eligible to receive certain tax benefits available to such certified business enterprises (*id.*).³ One of those benefits, the

³ Although the empire zones program expired on July 1, 2010, a business enterprise certified pursuant to Article 18-B of the General Municipal Law as of June 30, 2010 may continue to claim the QEZE tax reduction credit for the remainder of its benefit period, so long as it meets the relevant eligibility requirements.

QEZE tax reduction credit, provides for a credit against taxes imposed directly on the QEZE or, where the QEZE is a disregarded or flow-through entity for tax reporting purposes, personal income taxes imposed on its owners (Tax Law § 16 [a]).

C. This matter concerns petitioners' entitlement to QEZE tax reduction credits that they claimed for tax years 2015 and 2016 as pass-throughs from Tessy Plastics, a New York corporation that elected to be treated as an S corporation for federal and state tax purposes. As such, its income and any applicable QEZE tax reduction credits pass through to its shareholders, including petitioner Roland Beck, the majority shareholder⁴ of Tessy Plastics. As a shareholder of Tessy Plastics, Mr. Beck claimed empire zone credits, including the QEZE tax reduction credit on the New York personal income tax returns that he and his wife, petitioner Susan Beck, jointly filed for tax years 2015 and 2016. On their personal income tax returns filed for tax years 2015 and 2016, petitioners claimed, among other credits, QEZE tax reduction credits in the amounts of \$770,670.00 and \$339,010.00, respectively. The Division conducted audit reviews of multiple empire zone credits that petitioners claimed on their 2015 and 2016 personal income tax returns and requested information regarding the calculation of the empire zone tax credits, including the QEZE tax reduction credits. Petitioners provided the information requested for tax years 2015 and 2016 and indicated that all income received from Tessy Plastics was included in their calculation of the QEZE tax reduction credit claimed for each year. By letter, dated December 5, 2017, sent to petitioners for tax year 2015, the Division stated that petitioners' QEZE tax reduction credit was reduced from \$770,670.00 to \$152,279.00, based upon its application of Tessy Plastics's reported BAP of 19.7475% to petitioners' QEZE income for such year. For tax year 2016, the Division sent a letter, dated April 4, 2018, to petitioners stating that

⁴ Mr. Beck, directly and through The Roland G. Beck Retained Annuity Trust, owned 67.1025% of the stock of Tessy Plastics in tax years 2015 and 2016.

petitioners' QEZE tax reduction credit was reduced from \$339,010.00 to \$72,436.00, based upon its application of Tessa Plastics's reported BAP of 21.3694% to petitioners' QEZE income for such year. The Division applied the BAP of Tessa Plastics as a component of the tax factor calculation and thereby reduced petitioners' QEZE tax reduction credits by \$618,391.00 and \$266,574.00 for tax years 2015 and 2016, respectively.

D. Tax Law § 16 (b) provides that the amount of the QEZE tax reduction credit "shall be the product of (i) the benefit period factor, (ii) the employment increase factor, (iii) the zone allocation factor, and (iv) the tax factor." Where, as here, the QEZE is a New York S corporation and the tax reduction credit claimant is an S corporation shareholder, Tax Law § 16 (f) (2) (C) describes the tax factor calculation as follows:

"Where the taxpayer is a shareholder of a New York S corporation which is a qualified empire zone enterprise, the shareholder's tax factor shall be that portion of the amount determined in paragraph one of this subdivision which is attributable to the income of the S corporation. Such attribution shall be made in accordance with the ratio of the shareholder's income from the S corporation allocated within the state, entering into New York adjusted gross income, to the shareholder's New York adjusted gross income, or in accordance with such other methods as the commissioner may prescribe as providing an apportionment which reasonably reflects the portion of the shareholder's tax attributable to the income of the qualified empire zone enterprise. In no event may the ratio so determined exceed 1.0."

E. Tax Law § 16 (f) (1) states in relevant part that: "The tax factor shall be, in the case of article twenty-two of this chapter, the tax determined for the taxable year under subsections (a) through (d) of section six hundred one of such article."

F. The present matter concerns only the proper calculation of the tax factor component of the QEZE tax reduction credits that petitioners claimed for tax years 2015 and 2016. Petitioners contend that the Division incorrectly applied Tessa Plastics's BAP in the calculation of the tax factor component of the QEZE tax reduction credits claimed for tax years 2015 and 2016. They

assert that the tax factor formula in Tax Law § 16 makes no reference to the BAP. Petitioners maintain that, as New York residents, all their income from Tessy Plastics is subject to New York personal income tax. Petitioners claim that they reasonably and accurately included all their proportionate share of income from Tessy Plastics in the calculation of their QEZE tax reduction credits pursuant to Tax Law § 16. They note that the zone allocation factor appropriately reduced the credit calculation for any QEZE activities in New York State, but outside of the empire zone. Petitioners contend that the Division's use of Tessy Plastics's BAP in the calculation of the tax reduction credit as a means of allocating income within New York State does not result in "providing an apportionment which reasonably reflects a portion of the shareholder's tax attributable to the income of the qualified empire zone enterprise" (Tax Law § 16 [f] [2] [C]).

Petitioners argue that the Division misconstrued the holding in *Matter of Purcell v New York State Tax Appeals Trib.* (167 AD3d 1101 [3d Dept 2018], *lv denied* 33 NY3d 913 [2019], *appeal dismissed* 33 NY3d 999 [2019]), to mean that an S corporation's BAP must be included as a factor in the calculation of the QEZE tax reduction credit. They claim that the facts in *Purcell* are starkly different from those in the present matter, and the Division failed to recognize the distinctions that render the application of the BAP to petitioners' tax factor improper. Specifically, petitioners note that the S corporation in *Purcell* received substantial income from construction projects in Virginia. In contrast, petitioners assert that all assets and employees of Tessy Plastics are situated within New York, and all of its income during tax years 2015 and 2016 was earned from economic activity in New York State. Petitioners maintain that Tessy Plastics's reported BAP of 19.7475% and 21.3694% for tax years 2015 and 2016, respectively, reflects the sale and shipment of products to out-of-state purchasers. Petitioners also note that,

while the taxpayers in *Purcell* claimed resident tax credits equal to the amount of income tax paid to Virginia, they received no resident tax credits based upon the income of Tessa Plastics. Given these differences, petitioners contend that, although the use of the BAP to limit the QEZE tax reduction credit was appropriate in *Purcell*, it is not appropriate here. Petitioners also contend that the Division's application of the BAP in all cases is inconsistent with the language of Tax Law § 16. They argue that the tax factor provision contains no requirement to exclude tax on income from sales outside New York and does not require the application of the BAP. Petitioners assert that the tax factor provision looks to the shareholder's, and not the S corporation's, portion of income that is allocated to New York. They maintain that, as New York residents, all their income from Tessa Plastics is subject to New York income tax. As such, petitioners argue that their QEZE tax reduction credits for tax years 2015 and 2016 should be based upon all their non-excluded income from the S corporation, not their share of the S corporation's income multiplied by the S corporation's BAP, as advanced by the Division.

G. The Division contends that it properly applied the holding in *Purcell* to the present matter. It further contends that the holding in *Purcell* requires an S corporation shareholder's QEZE tax reduction credit calculation to use the S corporation's BAP in computing the tax factor. The Division argues that *Purcell* is not limited to the circumstances of that case. It also asserts that, although referenced in *Purcell*, the claim of a resident tax credit is not relevant in computing the QEZE tax reduction credit.

H. The Division is correct, the holding in *Purcell* is controlling in this matter. In *Purcell*, the S corporation at issue was certified as a QEZE and was a New York corporation that constructed commercial buildings mostly in New York and Virginia using prefabricated systems that it manufactured within an empire zone (*id.*) As an S corporation, its income and any

applicable QEZE tax reduction credits passed through to its sole shareholder, a New York resident, and such income was reported on his personal income tax returns that he jointly filed with his wife (*id.*). The taxpayers then calculated the QEZE tax reduction credit using all of the S corporation's income including income derived from its operations in Virginia (*id.*). Upon review of petitioners' personal income tax returns for the relevant years, the Division determined petitioners had miscalculated the QEZE tax reduction credits because they did not exclude their out-of-state income when calculating the tax factor despite the fact that it was not "allocated within the state" pursuant to Tax Law § 16 (f) (2) (C) (*id.*). The Division then applied the BAP to determine the portion of the S corporation's income that was allocated within the state for each of the relevant years (*id.*). The question in *Purcell* was the same as the question presented here, that is, does Tax Law § 16 (f) (2) (C) "require . . . allocation of a New York S corporation's income for resident shareholders based on the BAP reported by the corporation" (*id.* at 1105).⁵

The court determined that interpreting the meaning of the phrase "allocated within the state" was a question of statutory interpretation requiring consideration of the language and legislative history without deference to the Tax Appeals Tribunal's interpretation (*id.* at 1103). The court acknowledged that a tax credit is a form of exemption from taxation and must be strictly construed against the taxpayer, with any ambiguity to be held against the exemption (*id.*). It then noted that a taxpayer seeking an exemption from taxation bears the burden of proving a clear entitlement thereto showing that its suggested interpretation is the only reasonable

⁵ During the period at issue in *Purcell* (2008 through 2010) and the years at issue here (2015 and 2016) the BAP was defined, generally, as the ratio of New York-allocated business receipts to total business receipts (Tax Law former § 210 [3] [a] [10] [A] [ii]). For BAP purposes, receipts from sales of tangible personal property were generally allocated based upon the location of the purchaser and receipts from sales of services were generally allocated based upon the place of performance (*see* Tax Law former § 210 [3] [a] [2] [A], [B]).

construction (*id.*). In rejecting the taxpayer's position, the court found that the Division's method of applying the BAP to the S corporation's income gave meaning to the phrase "allocated within the state," and concluded that eligibility for the QEZE tax reduction credit for shareholders of New York S corporations is based only upon income that is earned by such corporations within New York State (*id.* at 1105). The court concluded as follows:

"Allocation of a New York S corporation's income within the state to a nonresident shareholder's New York adjusted gross income is determined by application of the BAP reported by the corporation. When calculating QEZE credits, it is rational to interpret Tax Law § 16 (f) to require similar allocation of New York S corporation's income for resident shareholders based upon the BAP reported by the corporation" (*id.*).

The court noted that this interpretation ensures similar treatment of resident and nonresident shareholders of S corporations and ensures that QEZE tax credits are based upon economic activity that occurs within qualified empire zones (*id.*).

I. With respect to the interpretation of Tax Law § 16 (f) (2) (C) advanced by petitioners, i.e. that all of a resident shareholder's income from an S corporation is properly included in the numerator of the tax factor fraction, the court in *Purcell* expressly rejected such interpretation. This proposed interpretation is deemed "facially implausible and unreasonable" because it "impermissibly render[s]" the phrase "allocated within the state" as used in Tax Law § 16 (f) (2) (C) superfluous or meaningless (*id.* at 1104).

J. Petitioners argue that unlike *Purcell*, all assets and employees of Tessy Plastics are situated within New York and all income during the tax years at issue was earned from activity in New York State. This argument is unavailing. *Purcell* holds that the language of Tax Law § 16 (f) (2) (C) requires allocation of an S corporation's income based upon the corporation's BAP when computing the tax factor for a resident shareholder. As noted, the BAP was based solely upon business receipts during the period at issue in *Purcell* and the years at issue in the present

matter (*see* Tax Law former § 210 [3] [a] [10] [A] [ii]). As such, **Purcell** is not distinguishable based upon the location of the S corporation's assets and employees.

K. Petitioners point out that the taxpayer in **Purcell** claimed resident tax credits for income taxes paid to Virginia attributable to corporate income derived from construction projects in Virginia. Petitioners assert that this fact created issues of fairness and misuse of tax credits in that case that are not present in this matter and thus justify a different result. I disagree. As noted, **Purcell** analyzes Tax Law § 16 (f) in accordance with principles of statutory construction and does not rely on the fact of the resident tax credits in reaching its holding.

L. Petitioners note that form CT-604, by which corporations claim the QEZE tax reduction credit, does not request the BAP, and does not require such information to be reported to shareholders for their tax reduction calculations. Petitioners also contend that the Division's position in the present matter is contrary to its prior interpretation of the statute in a technical memorandum that states that the "income from the QEZE S corporation allocable to New York State is the QEZE S corporation income from New York state sources" (TSB-M-06[1]C *Qualified Empire Zone Enterprise [QEZE] Tax Credits* [February 2, 2006], p.18). Petitioners note that the memorandum does not assert that the BAP should be a factor in calculating the QEZE tax reduction credit. Given the precedent of **Purcell**, I accord petitioners' arguments regarding form CT-604 and the technical memorandum addressing QEZE tax credits little weight (*see also* 20 NYCRR 2375.6 [c] and 2375.8 [c]).

M. Petitioners contend that the Division's application of the BAP in the calculation of the tax factor undermines the express public policy of the empire zone program to encourage businesses to create employment and to invest in economically depressed areas. They assert that the goal of the QEZE tax reduction credit was to potentially eliminate all tax liability generated

by the business. Petitioners argue that contrary to that policy and goal, the Division's application of the BAP in the calculation of the tax factor effectively excludes tax attributable to revenue derived from employment and operations in the empire zone from the QEZE tax reduction credit. The holding in *Purcell* refutes petitioner's public policy argument.

N. For the foregoing reasons, in its computation of their QEZE tax reduction credits for tax years 2015 and 2016, the Division properly multiplied Tessy Plastics's BAP by petitioners' income from Tessy Plastics in calculating the tax factor component of such credits. Therefore, the Division correctly reduced petitioners' QEZE tax reduction credits by \$618,391.00 and \$266,574.00 for tax years 2015 and 2016, respectively.

O. The petition of Roland and Susan Beck is denied; and the Division's December 5, 2017 letter and the December 12, 2017 account adjustment notice, denying in part petitioners' claim for credit or refund for tax year 2015, and the April 4, 2018 letter, denying in part petitioners' claim for credit or refund for tax year 2016, are sustained.

DATED: Albany, New York
March 02, 2023

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE